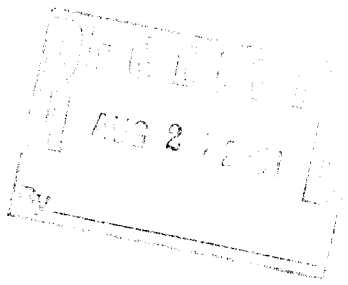
KATHLEEN CONNELL
Controller of the State of California
DIVISION OF COLLECTIONS

August 28, 2001



James Clark
Vice President of Government Relations
California Bankers Association
1121 L Street
Sacramento, CA 95814

Dear James,

Enclosed is a memorandum from the State Controller's Legal Office providing responses to questions raised by the Escheat Task Force. These answers represent the current position of the Controller's Office on the questions. Staff from the Bureau of Unclaimed Property Bureau will be reviewing current escheat instructions to insure the program information is consistent with these responses.

If you have any questions or wish to arrange a meeting to further discuss these issues, please call me at 322-9241.

Sincerely,

ROBERT SERTICH, Chief
Division of Collections

Bureau of Unclaimed Property
MAILING ADDRESS P.O. Box 942850, Sacramento, CA 94250-5873
3301 C Street, Suite 712, Sacramento, CA 95816 (916) 445-8318

ULCP-

State of California **Kathleen Connell, State Controller**

Memorandum

To : Walter Barnes
Chief Deputy Controller, Finance

Date: August 6, 2001

From : State Controller's Office
Ronald V. Placet
Senior Staff Counsel

Subject: UNCLAIMED PROPERTY QUESTIONS BY BANKER'S ASSOCIATION

The Escheat Task Force of the Banker's Association has asked several questions regarding unclaimed property issues and has submitted its proposed answers to those questions. For reference, these proposed answers are attached to this memorandum.

You have requested that we review the questions and answers and either concur with the proposed answers or submit answers of our own. The following review is based on the information presented and the specific questions. Our responses could change if the facts in any specific situation are different from those presented.

Account Fee Increases

"Q: If a financial institution decides to increase the monthly fees on an account and sends a change-in-terms notice to its customer, is the notice effective for escheat purposes if it is returned unopened by the Post Office?"

RESPONSE: We would agree that if the notice is undelivered due to an error by the financial institution, the notice is ineffective for escheat purposes. However, whether the notice is deemed effective when it is undelivered because of actions of the account owner or when other methods of notice are used would depend on whether the notice was given pursuant to a valid, enforceable contract or a statute other than the Unclaimed Property Act.[1]

"Q: If a depositor asks the institution to hold all statements and notices at his or her branch of account, and agrees to be bound by those notices whether or not (s)he picks them up, are the notices effective?"

RESPONSE: We concur with the proposed answer from the Banker's Association that it would depend on whether the depositor's agreement is a valid, enforceable contract under state law.[2]

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[1] CCP §§ 1513(a), (b) and (g), 1520; and 2 CCR §§ 1151, 1160 and 1162.
[2] CCP §§ 1513(a), (b) and (g), 1520; and 2 CCR §§ 1151, 1160 and 1162.

Pledged Accounts

"Q: If an account is pledged as collateral to the depository institution as security for a loan by the institution, who is considered the 'owner' of the account for purposes of CCP § 1513?"

"Q: What if the account is pledged to a third party? May the institution consider the circumstances of the pledge in determining whether the account is active?"

RESPONSE: We disagree with the Banker's Association's response to both of these questions. In both cases, the depositor is the owner of the funds unless (s)he fails to perform under the contract. The interests of the institution or third party are contingent and arise, if at all, only upon the failure of the depositor to perform in accordance with the agreement. The institution or third party would not appear to be an owner within the meaning of CCP § 1513 unless it could be established that the depositor did not perform pursuant to the agreement.

The funds deposited are used as security for the performance of the depositor under the contract. Implicit in such an agreement is the understanding that once the depositor has performed his or her obligations, the deposit will be released. Pursuant to the expressed language of CCP § 1518[3], the dormancy period begins to run on the date the funds become distributable or payable. Thus, the accounts pledged as collateral and held by the financial institutions become payable and distributable when the depositor has paid the loan or performed under the contract with the third party.

Blocked Accounts

"Q: Do blocked accounts escheat to the Controller if the owner fails to perform any of the activities described in CCP § 1513 (i.e., conducted a transaction, correspond in writing, or otherwise indicate an interest in the account)?"

RESPONSE: We concur with the proposed answers from the Banker's Association. The funds in a blocked account under a court order are assets held in trust for the potential beneficiaries of an estate. Once an order of the court is issued distributing the assets of the estate, the funds become payable and distributable within the meaning of CCP § 1518 and the court would no longer retain jurisdiction over the blocked account. Therefore, the dormancy period would begin to run. However, if the dormancy period has expired prior to the funds being put into the blocked account, then a court order is required for the funds to escheat to the State.

[3] In pertinent part, CCP § 1518 states: "All tangible personal property located in this state and subject to Section 1510, all intangible personal property, and the income or increment on such tangible or intangible property, held in a fiduciary capacity for the benefit of another person escheats to this state if after it becomes payable or distributable, the owner has not within a period of three years, increased or deceased the principal, accepted payment of principal or income, corresponded in writing concerning the property, or otherwise indicated an interest as evidenced by a memorandum or other record on file with the fiduciary." [Emphasis added]

In-Lieu Accounts

"Q: How should a bank treat funds that must be held in an account pursuant to state or federal law (e.g., funds deposited for the benefit of the state, in lieu of a bond to secure the depositor's performance)? In many cases, the depositor is not allowed to withdraw the funds, and a government agency is listed as the accountholder or the payee."

RESPONSE: We disagree with the Banker's Association's response.

The funds deposited are held in trust to secure the performance of the depositor. Implicit is the understanding that once the depositor has performed his or her obligations, the deposit will be released. Pursuant to the expressed language of CCP § 1518, the dormancy period begins to run on the date the funds become distributable or payable. With respect to the accounts held in trust, an account is not distributable or payable until the governmental agency no longer has an interest in the account.

Cashier's Checks

"Q: If a banking or financial organization issues a cashier's check, regardless of its purpose, does the cashier's check escheat to the State as provided in California Code of Civil Procedure Section 1513(d)?"

RESPONSE: We concur with the proposed answer from the Banker's Association.

Early Withdrawal Penalties

"Q: May a banking or financial organization assess an early withdrawal penalty to a time deposit withdrawn prior to maturity due to the funds escheating to the State of California?"

RESPONSE: We disagree with the proposed answer. It has been the position of this office for sometime that when time deposits are forced to be withdrawn before their maturity date because the funds escheated to the State, the deposits are not subject to early withdrawal penalties.[4]

Federal regulations provide that time deposits may be paid before maturity without imposing early withdrawal penalties. For example, early withdrawal of time deposits is not subject to withdrawal penalties upon the death of the owner or when the owner is declared legally incompetent. In addition, a time deposit is not subject early withdrawal penalties when the time deposit is withdrawn within ten days after a specified maturity date, even though the deposit contract provided for automatic renewal at the maturity date.[5]

[4] This opinion has previously been expressed. (In a February 24, 1994 letter and a June 5, 1997 memo from the Chief Counsel.)
[5] 12 CFR 204.2(c)(1)(i), note 1

It would appear that penalties for early withdrawal are applicable only when the owner closes the time deposit account prior to maturity. When the depositor no longer controls the funds, as is the case when a depositor dies or is declared legally incompetent, the early withdrawal penalties do not apply. Similarly, when the owner abandons the property, it may be presumed that the owner no longer exercises control over the funds on deposit. Thus, when abandoned time deposits escheat to the State of California for safekeeping for the rightful owner, the funds would not be subject to early withdrawal penalties.

Inactive Savings Accounts

"Q: Under what terms and conditions, if any, may a banking or financial organization cease the payment of interest to an inactive savings account?"

RESPONSE: We concur with the introductory section of the proposed answer from the Banker's Association.

We also concur with subsection (a) of the association's proposed answer. Under a valid, enforceable contract with its depositors, a bank or financial institution could credit interest to savings accounts only at the close of a quarter and, upon closing of an account prior to the end of a quarter, does not credit interest for a portion of the quarter. Therefore, upon closing of an account prior to the end of a quarter, the institution or bank would not under the Unclaimed Property Law be obligated to report interest for a portion of the quarter.[6] The SCO would have the same rights as the depositor. If the depositor would not receive interest for this period upon closing the account, then SCO would have no greater rights to demand payment of interest.

We disagree with subsection (b) of the proposed answer. CCP § 1513 requires any savings accounts "together with any interest" to escheat to the State when the account is inactive[7] for more than three years. It is clear that the legislative intent was not only for an item to escheat, but also any interest that accrued to that item. Furthermore, this section states that no banking or financial organizations may "discontinue any interest or dividends" on any savings deposits, on any funds paid toward purchase of shares or other interest, or on any deposits, because of the inactivity contemplated by that section.

The interest is paid and payable by the holder because (s)he has possession and use of the funds. That was the parties' intent and purpose and it is not changed by the fact that the funds are reported to the State. If the owner claims the funds from the bank after they are reported to the State, but prior to their delivery to the State, the bank or financial institution would undoubtedly pay interest to the date of

[6] The holder would be required to include as part of the report filed pursuant to CCP § 1530 either a copy of valid, enforceable contract authorizing such discontinuation of payment of interest, or the citation of the statute which authorizes such discontinuation of payment of interest. 2 CCR § 1170.

[7] 2 CCR § 1153: "inactivity" means the non-occurrence of any of the events or acts described in (1), (2) or (3) of subdivision (a) or (b) of CCP § 1513.

remittance to the owner. In like fashion, the bank should pay interest to the date of remittance to the SCO.

Finally, since the State has a statutory right to collect interest that has escheated, the release or surrender of such a right without adequate consideration would constitute a gift of public funds in violation of Article XVI § 6 of the California Constitution.

Attachment